

MID-TERM REVIEW OF THE SIXTH NATIONAL SOCIO-ECONOMIC DEVELOPMENT PLAN (2006-10)

EXECUTIVE SUMMARY

OBJECTIVES OF THE MID-TERM REVIEW

The 6th Plan (2006-10) is currently in its fourth year of implementation. The mid-term review aims to assess achievements and progress over the last three years and identify challenges in implementation. It is expected that results from the review will help introduce necessary corrections in the remaining years to meet the overall 6th Plan objectives and draw lessons for the formulation of the 7th Plan (2011-15) that will help improve service delivery, achieve the MDGs by 2015, and enable the country to graduate out of the LDC status by 2020.

ANALYTICAL FRAMEWORK

For a comprehensive and objective assessment of progress of implementation of the 6th Plan, the mid-term review addresses four sets of issues with accompanying analytical questions.

- Priorities – Are the priorities right to achieve the overall Goals of the 6th Plan? To what extent are the priorities in line with the MDGs? Based on these priorities can Lao PDR graduate from the LDC status by 2020?
- Resources – Has the money been allocated for the priorities? Are sufficient resources made available to achieve the desired outcomes?
- Implementation Process and Institutional Mechanisms – How is the Plan implemented? Do we have the necessary mechanisms for effective implementation such as the legal and regulatory framework; decentralisation; budget allocation; monitoring system, etc.? To what extent do the provinces reflect national priorities in their budget plans/requests?
- Progress – Is the implementation on track to meet the desired outcomes?
- Challenges – What constraints affect progress? What challenges need to be addressed for the remaining years of the 6th Plan? What are the priority areas for the 7th Plan?

DATA SOURCES

Data from a number of sources were used to address the analytical questions. These include:

- Draft Mid-term Review Report prepared by MPI
- Progress reviews/reports prepared by line ministries
- Background Papers prepared by development partners at the request of MPI
- Official statistics collected from different line ministries
- Review of Annual Plans, budget documents, official Gazettes
- Data and results of surveys conducted during the period
- Meetings with officials from line ministries and donor partner representatives to clarify issues and fill knowledge gaps.

MACROECONOMIC ISSUES

Overview of economic performance

Lao PDR achieved rapid growth over the first three years of the 6th Plan with an average annual GDP growth rate of 8.1% during 2005/06-2007/08 against the target of 7.5%. ***The average GDP per capita has already exceeded the Plan target of US \$700 two years ahead of schedule.*** All sectors have also so far exceeded their average annual Plan targets - agriculture and forestry grew at 3.9%, industry at 14.8% and the service sector at 8.5%. The resource sector (energy and mining) contributed about one-third of the overall growth of the economy. The non-resource sector (plantations for agricultural crops and industrial forestry, tourism, food and non-food processing industries) grew at 4.5-5% per annum.

The economy continued to industrialize and modernize during the 6th Plan. The declining contribution of agriculture to GDP (from 32.1% in 2005/06 to 29.7% in 2007/08) is matched with an increasing share of manufacturing and service sectors. However, Lao PDR remains a predominantly rural economy. The share of agriculture and forestry in GDP is not declining fast enough and may even increase. The relative shares of the other two sectors have also changed little in the 6th Plan period and the industry sector is unlikely to increase its share by almost 9 percentage points in the remaining period to achieve the 2010 target. The sectoral growth rates achieved until now will need to be sustained over a considerable period of time before they can begin to alter their relative contributions to the overall economy.

Monetary Policy

Helped by favorable oil and food prices, and appreciation of the kip against the dollar, ***inflation remained within the target range of 6-6.5% during the first two years of the 6th Plan.*** But increasing oil prices, fluctuations in local food prices, and rising non-food prices pushed inflation to around 7% in the first 7 months of 2007-08. Given recent regional and international trends, the Plan target for 2008/09 has been revised to keep inflation below 10% and the Government has tasked several agencies to help combat inflation.

The overall money supply (M2) increased significantly during 2006/07 due to the increase in foreign currency holdings of the Bank of Lao PDR. Foreign currency holding is valued at 6.7 months worth of imports which is expected to increase in 2008 driven by high prices for mining and agricultural exports, tourism receipts and FDI inflows.

Fiscal Policy and Expenditure Management

The government's fiscal position continued to strengthen as revenue targets were achieved for a second consecutive year. ***As proportion of GDP, revenue mobilization by the Centre increased by 1.5 percentage point in 2005/06 – 2007/08. In actual terms this translates to an increase in revenue of 2,000 billion kip during this period.***

The new State Budget Law promulgated in 2007 addresses the weaknesses in the inter-governmental fiscal framework. Key reforms include centralizing the Finance, Customs and Tax departments; developing a new fiscal transfer system; establishing greater control of

public finance resources; and aligning policies to the budget. The new Audit Law in July 2007 ensures that the State Audit Office now directly reports to the National Assembly.

Budget Balance

The total revenue in the first three years of the 6th Plan was estimated to be 14,834 19,093 billion kip which equals 55% of the target. Customs duties and taxes together account for nearly two-third of total budget revenue. The introduction of the value added tax (VAT) early next year with a single rate, broad coverage of goods and services, and restricted exemptions is expected to increase revenues as well as address many of the weaknesses in the existing turnover tax.

The estimated total public expenditure during the period 2005/06-2007/08 is 22,481 billion kip. After three years of the Plan period total revenue and expenditure are less than half the Plan target but this is not a cause for concern as revenues are likely to get a boost soon after Nam Thien 2 goes on stream by end-2009. The year-on-year budget deficit (or cash balance), as % of GDP, is within the 3-5% range in 2005/06-2007/08 and is estimated to fall to decline from 3.8% in 2005/06 to 2.1% in 2007/08 with an expected increase in revenues as a result of the introduction of VAT.

Domestic expenditure, as % share of GDP, is expected to increase to 13% and will push the overall expenditure to above 19% in 2007-08. Overall donor-financed expenditure is expected to decline from 8% of GDP in 2005-06 to 6% by 2007-08. In absolute terms and at current prices, donor-financed expenditure declines marginally by about 50 billion kip during 2005/06-2007/08. In dollar terms, donor-financed expenditure shows an increase of US \$40 million during 2005/06-2007/08 because of the appreciation of the kip against the US dollar.

Total expenditure in education and health is estimated to increase by 17% during 2005/06-2007/08. This is because of an estimated 57% increase in domestic spending; donor funding (in billion kip) in these two sectors is estimated to decrease by 9% during this period. However, in dollar terms, donor funding increases by 6% because of appreciation of kip against the dollar, which suggests that it is important to develop a suitable system to carefully track ODA.

Total expenditure on agriculture and infrastructure is estimated to decrease by 18% during 2005/06-2007/08. Much of this is due to a reduction of 510 billion kip in donor outlay in this period. In dollar terms also there is a decline of 17% in donor funding for agriculture and infrastructure in this period and ***this trend needs to be reversed for Lao PDR to graduate from the LDC status by 2020.***

Data Issues

A number of factors make it difficult to reconcile the public expenditure data. MPI records donor commitments in US dollars while MOF records actual disbursements in billion kip. Because of exchange rate variations figures in the two different currencies do not always tally. Further, donor disbursements may not always follow commitments, or do so with a time lag, many donors do not provide accurate and up-to-date reports of bilateral aid, and increasingly, some donors provide aid that is not recorded and thus, remains off-budget.

Financial and banking sector

While the financial sector has grown, it remains small and dominated by banks. Non-bank financial institutions are estimated to constitute less than 5% of total financial sector assets. Assets in the financial sector at end-2006 were estimated at about 27% of the GDP, which represents a very small increase in recent years. Deposits exceed loans in the banking system by approximately 2:1 and loans are a small share of aggregate banking sector assets.

The government has initiated several important measures to strengthen the regulatory framework for banking and micro finance leading to performance improvements in 2007. Management changes and prudent lending practices have lowered non-performing loans (NPLs) on new lending and reportedly improved profitability; new private banks have been allowed entry and investment in the private Vientiane Commercial Bank by IFC and ANZ Bank will help reduce the dominance of SOCBs; and the capital adequacy requirement for the banking sector was set at 8% in line with Basel Core Principles.

Banking supervision is improving. Bank boards no longer include an official from the BOL, and are chaired by an MOF representative instead. The Law on Commercial Banks promulgated in 2007 provides a transparent, clear and easy licensing procedure for establishing a bank, a level playing field for domestic and foreign banks and no discrimination between private and state-owned banks.

Implementation of Investment Projects

The Public Investment Program (PIP) is the Government's instrument to plan and allocate capital investments in the public sector for achieving the 6th Plan objectives. It is an integral part of the national budget formulation process and accounts for almost half of the total Government (public) expenditures. PIP is also an important tool for the Government to manage aid, most of which is provided in the form of project support. PIP provides a consistent framework within which aid agencies can concentrate and coordinate their efforts.

ODA, in the form of grants and concessional loans, plays an important role in both the overall public expenditure and PIP. Over the last 2.5 years, ODA projects comprised, on average, 84% of the total PIP budget. In absolute terms *ODA has been more or less constant during 2005/06-2006/07 and is likely to register a small (5-7%) increase in 2007/08.* However, *only about 65-70% of the total ODA is recorded as aid from many ~~bilaterals~~ and non-DAC countries stays off-budget.*

Foreign investments in Lao PDR are expected to be robust in the 6th Plan period. Although the approved foreign investments has declined by more than half in 2006-07, actual investments are expected to rise due to new investments and existing large resource and non-resource projects. *Actual FDI inflows are estimated at about US \$950 million in 2007 showing a 60% increase over the previous year.* Growth was mainly driven by new, large investment projects, such as mining, non-resource industries (food and beverage, agro-processing industries and manufacturing), agriculture, services, and ongoing construction of three hydropower projects (NT2, Nam Ngum 2 and Xekaman 3).

Several new large projects worth over US \$1 billion were approved in 2006-07 in agriculture (plantations and forestry), trade, services (shopping malls, entertainment, tourism and

banking services) and industry (hydropower and mining projects). *The structure of Lao PDR's investments continues to diversify, although large projects still constitute the predominant part of the total FDI.*

A Combined Investment Law is being developed to improve investment attractiveness. It will not differentiate between domestic and foreign investors and promote a level playing field. The new law is scheduled to be considered by the National Assembly in end-2008. *Approval of the Negative List (Conditional List) of Business Activities under the Enterprise Law is expected soon and will help simplify business entry regulations.* An Enterprise Registration Office has been created to implement the new simplified business registration procedures. With support from the donor community, MoIC plans to introduce a new business registration system by 2010 and create a national business registry containing information on all registered enterprises.

THEMATIC AND CROSS-CUTTING AREAS

Poverty reduction and rural development

Poverty reduction is an outcome of several cross-cutting areas. A key challenge in tracking poverty indicators is that these indicators change slowly over time. There is little change on a year-to-year basis in the head count ratio, malnourishment, enrollment or mortality rates. Data collection for these indicators takes place with the help of sample surveys once every three to five years. For many of these indicators, the most recent published data is either at the start of the 6th Plan or even before and hence can be used only as a baseline, and not to review progress.

There has been considerable progress in recent years in poverty reduction and estimates from the last sample survey conducted in 2007 suggest that poverty head count ratio has dropped to less than 25%. Thus, the country may have achieved the 6th Plan poverty reduction target two years ahead of schedule. However, the target of abolishing seasonal hunger by 2010 seems to be difficult as nearly one in five persons still lacks sufficient access to food.

The ratio of malnourished children under-five are targeted to fall below 30% by 2010. Estimates suggest that *despite considerable efforts, 37% of children under-five years of age were underweight in 2006.* There has been little improvement in this indicator since 1990 and urgent attention is required by both government and the development community. Progress on primary enrolment rate and access to clean water indicators seem well on-track, though the extent of the forest cover is unlikely to reach the 50% level targeted by 2010.

The poverty reduction strategy of the 6th Plan consists of five components. Lao PDR's achievements in the first three components of the strategy: extension of economic opportunities; provision and use of basic social services; and promotion of participation and empowerment are discussed under specific heads in the review. The following sections analyse the last two components of the poverty reduction strategy viz. "ensuring the security of people and property" and "development of the poorest areas."

Poverty focussed national programmes

UXO Clearance – MOLSW along with UXO Lao has conducted community awareness and risk education activities in 1,872 villages with 410,211 participants. Surveys were conducted and data collected on UXOs in different areas in 3,392 villages; a total of different types of 43,443 UXOs were found; and removable UXOs were destroyed in 2,383 villages.

UXOs were cleared from a total area of 9,963.8 ha and a total of 98,713 UXOs were found and destroyed; 491,237 local people benefited from the project. Over the past two years, there were 101 accidents with 164 victims, of which 57 were killed and 107 injured.

The work to develop a national database and data collection system on UXO accidents is underway at the NRA Office and is expected to be fully operational by December 2008. Preliminary analysis suggests that on average there have been 300 UXO victims per annum over the last decade. The initial target set was based on unreliable data and was unrealistic.

Development of poorest areas - *The Village Development Fund (VDF) is used actively and efficiently and the Government has approved 41.7 billion kips from 2003/04 up to the present to provide development funding at village level* to encourage and promote poverty eradication through plantation, animal-raising, handicrafts, trading and other income generating activities. *A total of 459 VDFs have been established with total of 22,803 households and covering 17 provinces across the country.*

So far, a total of *58 Kum Ban Plans have been prepared in 51 districts with 683 projects in the four sectors of Agriculture and Forestry, Health, Education and Infrastructure and an estimated budget of 319 billion kip for 2006-10.* Prior to 2008/09 there were no public investments in these projects, or at least none that was specifically recorded. For 2008/09, GOL will allocate 36 billion kip to the identified projects, focusing on those districts where the Poverty Reduction Fund does not operate. A strategy to seek ODA funding for the projects is in the process of being developed.

The National Leading Committee for Rural Development and Poverty Eradication (NLCRDPE) was established at the centre to build a foundation for rural development in all aspects at provincial and district levels. To date, provincial and district Rural Development and Poverty Eradication offices have been established as the centre of coordination with other sectoral offices in planning, prioritisation of projects, support, monitor, evaluation and periodically reporting on the progress on rural development and poverty reduction to each sector accordingly.

Land allocation (with agricultural area of 4.21 million ha and forestry area of 6.65 million ha) has been completed for 443,523 households in 7,130 villages. *Areas of slash-and-burn forest for unplanned rice cultivation have been reduced from 14,400 ha in 2006 to about 8,025 ha in 2007* due to the expansion of industrial trees plantation which increased up to 6,000 ha in some provinces such as Luangphabang, Oudomxay, Bokeo, Bolikahmxay, Savanakheth, Champasack and Saravan. In addition, people have changed their livelihoods to raise animals and for other production.

The Poverty Reduction Fund (PRF) promotes poverty reduction directly, and has received credit agreement from World Bank of US \$19.8 million and some Government counterpart

funds. In 2003-08, activities have covered 21 districts in Huoaphan, Xiengkhuang, Savannakhet, Champasack and Saravan. There are a total number of 744,140 beneficiaries in 161 village groups across 1,913 villages with 2,067 projects worth more than 168 billion kip.

By 2007, education network in remote areas improved gradually and 94% of villages have a primary school increasing primary school enrollment. Public health service has improved in the rural areas as the villages and village groups were defined as focal areas in public health service and healthcare. At present there are 770 health village centres which cover 96% of the villages. People with access to safe drinking water has gone up to 58% while 48% of total households use permanent latrines.

Gender equality

Lao PDR has ratified various international Conventions including the Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW, 1981), and the Beijing Platform for Action (1995). The Government is also committed to implementing the Millennium Development Goals (MDGs) which includes gender equality and women's advancement.

Under the leadership of LaoNCAW, ***a number of Ministries have begun to mainstream gender into their activities***, while some are in the process of setting up teams to undertake the process. Sub-Commissions for the Advancement of Women (Sub-CAWs) have been established pursuant to Government Instruction in units within Ministries and equivalent organizations, as well in the provinces with a view to ensuring more practical implementation of gender mainstreaming.

All the same, women continue to be disadvantaged in their daily lives and gender gaps persist in a number of key social and economic development indicators such as health, education, agriculture, and government representation. Although at national level there has been an overall improvement in indicators for gender equality and empowerment of women, the challenge lies in identifying and addressing the causes of the great disparities that exist between urban and rural areas and between different regions.

It is important that the empowerment of women and contribution to public life is encouraged at all levels, including the village. Currently, stereotypical attitudes continue to affect girls in the family, school and society. Females experience an unfair distribution of labour inside the home and men are usually considered the head of households and the decision-makers at the domestic and village level. Consequently, women and girls are restricted in their ability to access education and gain less exposure to and contribute less to village and community development despite playing a significant social and economic role.

Governance

The Government's Strategic Plan for Governance outlines the key initiatives to be undertaken in the sector to implement the targets of the 6th Plan. The Strategic Plan informs government agencies and the communities of the initiatives being undertaken for better delivery of services, and aims to facilitate dialogue between Government and development partners for efficient coordination, use and review of resources. It covers four key areas of (i) public

service improvement, (ii) people's participation, (iii) rule of law and (iv) financial management.

Public service improvement

The Government has concentrated on the improvement of the roles, functions, duties and organizational structure and has appropriately undertaken personnel deployment and appointment. At central level, efforts have been made to enable Ministries to perform mainly their macro management roles, to apply the principle of decentralization, assignments of work, authority and responsibilities to the local level and technical units. The roles, functions and rights of a number of Ministries have been reviewed. Some specific tasks were transferred to Ministries and equivalent agencies to ensure more efficient management. A number of new organizations have been established with the specific aim to respond to the actual work.

Civil service management in the country has been improved and developed in a systematic manner by moving toward management based on principles, regulations and methodology and in compliance with the restructuring guidelines. The total number of Government personnel in the country is 104,726 in 2006/07 compared to 99,659 in 2005/06 which is an increase of 5%. More than half the personnel are deployed at the district level and one-third at the provincial level.

The management of civil service applies, increasingly and continually, the merit-based system and has gradually discouraged the application of the spoils principle. Presently, civil servants are trained and upgraded in terms of knowledge, skill, qualifications and ethics for serving the people.

Peoples' participation

Lao PDR is committed to ensuring that the Lao people are closely consulted in all areas of decision-making and are able to participate fully in all areas of the socio-economic development of the country

Reporting on the status of implementation of the 6th Plan is presented to the National Assembly at each session. These reports were detailed in the local newspapers and demonstrate that the Government supports greater transparency of its performance – even when the performance (in particular, revenue performance) did not meet its target. There has been a growing level of community feedback incorporated into national newspapers which actively seeks comments on a range of topics. Increasingly the media is providing coverage on issues (including corruption) which were previously considered too sensitive for disclosure. The State Inspection Authority (SIA) receives complaints from the public and in recent years the number of complaints received has risen from 240 in 2001/02 to 408 in 2005/06, indicating a growing acceptance by the public of the SIA as a legitimate and responsive avenue.

Rule of Law

The Government has paid attention to the improvement of various legislations and regulations by establishing and developing Laws and State Management in many areas. Some of the key legislations during the 6th Plan period relate to:

- Approval of the Negative List (Conditional List) of Business Activities under the Enterprise Law in late 2007. It is expected that the GOL will officially issue the Negative List in the coming months. An Enterprise Registration Office has been created to implement the new simplified business registration procedures. With support from the donor community, MOIC plans to introduce a new business registration system within the next 2 years and to create a national business registry which contains information on all registered enterprises.
- The successful revision of the Mining Law is the fundamental corner stone of strengthening of the mining sector.
- Implementing decree of the Tourism Law includes provisions on the role and responsibilities of the LNTA, institutional framework and funding, quality and standards and licensing procedures for service providers.
- To facilitate cross-border trade, GOL reduced the number of check points to immigration, customs and quarantine. A new Commercial Banks Law was endorsed and amendments to the Presidential Decree on Foreign Exchange and Precious Metals were adopted in 2007.
- The Water Supply Law was submitted to the National Assembly in 2008, to provide a legal framework for the sector and improve construction and regulation of water supply systems, water quality controls and promote private participation.
- GOL has revised the 1994 Budget Law and Treasury Decree. The revised State Budget Law addresses some of the important issues regarding the budget cycle; the powers, roles, and responsibilities of key legislative and executive bodies in the budget planning and execution process; and central/local fiscal assignments and transfers. A revised Treasury Decree has also been prepared.
- The State Budget Law defines principles, regulations and measures in planning, implementing, evaluating, and auditing the State budget to transparently manage budget revenues and expenditures with the aim of constructively contributing to the continuous and sustainable growth of national socio-economic development.
- All budget revenues and expenditures have been fully centralised and accounted for in the State budget through the National Treasury on the basis of nationwide unified laws and regulations. No revenues are to be retained outside the budget system and no funds may be established without proper authorization.
- A new audit law has been drafted to strengthen the role of the state audit and to clarify its responsibilities and reporting relationships. It strengthens the role of the state with the SAO becoming an independent body reporting to the National Assembly. It outlines the objectives of state auditing, the principles of audits and auditing standards, and a code of ethics for auditors.

Financial management

There have been significant improvements in public expenditure management in recent years. The Ministry of Finance has undertaken various steps to improve transparency and accountability in expenditure planning and management. This included revision of the budget law, new mandate of the national treasury, development of a medium term expenditure framework (MTEF) and modifying the current budget nomenclature and chart of accounts. The reporting system of the budget execution has been enhanced by ‘rolling out’ the computerized accounting system.

Presently, fiscal planning and budget preparation display four key problems:

- a lack of realism in the fiscal forecasts, leading to unpredictable spending by way of arbitrary cash rationing;
- no mechanism for ensuring that provinces reflect national priorities in their budget plans;
- a budget process that is fragmented institutionally and by type of expenditure; and
- an overly compressed budget cycle.

Other problems include the continuing off-budget funds, deficiencies in the budget nomenclature, little systematic monitoring and evaluation of budget execution, procurement planning that is not integrated effectively into the budget preparation process, and the short-term horizon of the budget process. Recent GOL actions have made budget targets for revenues more realistic and have expanded the period over which the budget is prepared. A revised chart of accounts and budget nomenclature is being developed and is expected to be completed by 2008.

As part of the financial management reform the government, in collaboration with development partners, has developed the Public Expenditure Management Strengthening Program (PEMSP) covering key government initiatives, planned so far, until June 2009. The program focuses on strengthening the management systems and capacities of MOF, MPI, SAO, line ministries and provincial/district finance departments. The program has five components:

- Fiscal Planning and Budget Preparation
- Budget Execution, Accounting and Financial Reporting
- Local Government Financial Management
- Financial Legislation and Regulatory Framework
- Capacity Building

Trade

The National Export Strategy (NES) and the Diagnostic Trade Integration Study (DTIS) guide the implementation of the 6th Plan Trade Strategy. The DTIS identified five priority areas for development assistance for Laos:

- Export Competitiveness
- Trade Facilitation
- Business Environment

- Trade Policy, Trade Agreements and Global Opportunities
- Trade Opportunities for the Poor

Within these priority areas, a number of important trade related projects have been initiated by the Ministries of Finance; Industry and Commerce; Communication Transport Posts and Construction (CTPC); and Agriculture and Forestry over the last 2 years in partnership with key DPs. With the growing importance of aid-for-trade, there is a marked increase in the amount of ODA being channeled or committed for improving trade in Laos and underlines the urgent need for stronger inter-agency and government-donor coordination.

Through the WTO Integrated Framework (IF) process and with the support of the IF Donor Facilitator, MOIC has set up mechanisms for effective management and coordination of Trade Related Assistance (TRA). The Ministry is in the process of establishing a permanent National Integrated Framework Governance Structure (NIFGS), a multi-agency entity consistent with the IF and the Vientiane Declaration, to coordinate ODA in the trade sector.

Export-Import Balance

Overall, Lao exporters have performed well in recent years. *Exports have increased at an average annual rate of 29% since 2005-06 and the total value reached US \$2.77 billion in the first three years, equal to 79.57% of the 6th Plan target.* Apart from the mining sector which accounts for close to 60% of the value of annual exports, export growth was driven by agriculture (mainly coffee and maize) and garments, with both of these industries increasing by over 20%. Exports from processing and service industries increased during the past ~~two~~ three years, even as the export of electricity and wood products declined marginally and gold exports dropped by over 20% due to a significant decrease in production in 2007. Still, exports from Lao PDR are much less than that from other countries in the region.

Total imports in the past 3 years reached US \$2.84 billion, or equal to 63.14% of the Plan target with an average increase of 14.51% per year. The value of imports in 2007-08 is expected to reach to US \$1,001.81 million. This increase is largely driven by increased investment imports for large resource projects (mining and hydropower accounting for about 45% of total imports), agriculture (plantations), processing industries, trade and services. Capital imports constituted almost 70% of total imports in 2006-07. Imports of raw materials increased by almost 30% and consumption products increased slightly. The overall import trends are in line with the 6th Plan import targets.

The 6th Plan aims to prioritize imports of material, equipment and advanced technology for industrialization to enhance competitiveness of locally-produced goods. So by 2010 the composition of imports is expected to shift towards import for investment projects from raw materials and fuel.

Lao PDR's key trading partners remained largely unchanged in 2006-07, and *key export markets include the ASEAN countries (Thailand, Vietnam, Malaysia), the EU, China, and Australia.* The share of Lao exports to Thailand decreased from about 50% in 2005-06 to around 30% in 2007. Exports increased rapidly from 11 to 16% to Vietnam and from five to 11% to China. Recently, Lao exports to the US have increased but the overall value is low (just over 1% of total exports). *Most imports to Lao PDR still come from ASEAN countries (about 68% from Thailand and 13% from Vietnam), China (7%), EU (3%) and other countries account for the remaining 9%.*

Lao PDR has gradually been integrating into the world economy since 1989, with accession to ASEAN in 1997. ***Lao PDR has signed a number of agreements to promote trade. These include an investment promotion agreement with Japan, and an economic cooperation agreement with South Korea to promote cooperation in the areas of trade, investment and services.*** The 6th Plan objective is to fully implement the integration roadmap and meet the commitments to become a member of the WTO and multi-lateral regional bodies such as AFTA and GMS. Many items are still under consideration for tariff reductions and it is unlikely that tariffs will be completely reduced to 0-5% by end of 2008 which is the deadline. At the same time, ***capacities of institutions and staff will be adjusted and strengthened to meet the modernization requirements and to comply with WTO regulations.***

The number and value of investments of ASEAN countries in Lao PDR have increased each year since 2004. The top three ranking investments are from Thailand, Vietnam and China. ***Direct investment from foreign countries, in hydropower, mineral and tourism sectors, more than doubled from US \$1,245 million in 2005 to US \$2,700 million in 2006.*** Currently, ASEAN has carried out the improvement of Agreement on ASEAN's Investment Areas (AIA) to be ASEAN Circle Investment Agreement (ACIA) in order to be consistent with the new situation and increase confidence for both domestic and foreign investors.

The Government continued to make progress on WTO accession, with the third working party held in Geneva in November 2007. MOIC updated the legislative action plan and discussed the Initial Offers for Goods and Services with negotiating partners during the working party meeting. Work on formal responses to the questions raised by bilateral and multilateral negotiating partners are ongoing. Overall, the preparation for WTO membership is moving from the stage of clarification to the stage of negotiation to have the multiparty (regulation aspect) and bilateral (Initial Offers on Goods and Services) agreement.

Private sector development including SMEs

Sustaining growth is one of the key objectives and revenue mobilization is one of the first priorities of the Government and it attaches considerable importance to the role of the private sector in the country's economic growth. Private sector development (PSD) is emphasized as one of the drivers of export-led growth in the 6th Plan. The Government has taken a number of proactive steps to improve the business and investment climate in the country.

Since its inception in 2005, the Lao Business Forum (LBF) has helped improve the private sector business environment by providing a platform for dialogue and information sharing with existing and potential investors. The Forum has played an important role in streamlining investment procedures for both domestic and foreign investors, strengthen enforcement of existing laws and regulations and make Lao PDR attractive for investors.

Provincial public-private dialogues with the private sectors have been introduced in cooperation with the GTZ on a pilot basis in Champasak, Savannakhet, Luang Prabang and Luang Namtha to improve the business and investment climate in the provinces.

The main challenges to private sector development are to sustain current growth in manufacturing and services; to ensure that the private sector can produce goods and provide services that meet regional export demand; and to expand the domestic market. To

meet these challenges, Lao PDR needs to exploit the full potential of the private sector to invest, expand, create jobs, and increase productivity. This requires a better understanding of the barriers to the growth and productivity of firms in the key sectors, including policies to address the constraints, in order to improve the investment climate.

The SME Development Strategy was formulated to support the implementation of directions and policies of the government for the promotion and development of small and medium sized enterprises in accordance with the Prime Minister's Decree No. 42/2007. Presently, there are an estimated total of 134,000 SMEs (employing up to 99 employees) representing about 95% of all economic establishments in the country. Of this, approximately 18% are engaged in manufacturing and processing, 44% in trading activities and 38% in the service sector. The majority are micro and small enterprises employing a maximum of 2 people in the informal sector (not formally registered) and less than 10 people in the formal sector (legally registered). Together, the SMEs employ about 400,000 people.

Agriculture and agro-processing will remain important not only for meeting domestic demand but also for exports to a rapidly growing region. Manufacturing and tourism firms continue to face significant constraints to investment, productivity, and growth, and these will have to be addressed. Rapid growth of the private sector is constrained by three main factors:

Access to finance

Lao PDR has made great strides in the 6th Plan period to improve and grow its financial sector and although the financial sector is developing rapidly, *access to finance is still one of the major constraints for Lao businesses, especially for SMEs*. Despite the promulgation of the law on Commercial banks, many Lao private firms without any FDI have limited or no access to credit. As a result some of these firms are unable to invest enough and remain too small, unable to take advantage of economies of scale, less able to compete with imports, and less able to make investments to protect the environment.

Availability of skilled manpower

Having a well-educated and abundant labor force is essential for the development of the Lao economy in general, and will be an important factor in attracting new investments. Investment in education should be a priority, as this will have a direct impact on the development capability and skills in the work force. Tourism firms highlight inadequate skills and education of workers as the most important impediment to doing business in their sector.

Regulatory framework

Although the private sector is growing steadily, the required procedures are complex and still open to discretion of responsible officials. *It takes about 190 days to start up a new business* and is also expensive. This discourages private sector development. A more favourable environment for the promotion of the private sector and the attraction of FDI will be created by primarily improving the legal system and maintaining socio-economic stability. Additionally, existing regulations, laws and procedures need to be modified and the administrative application system for business activities of enterprises need to be reformed to accelerate the process of setting up a business.

There are concerns within the business community related to the decree of implementation on secured transaction law which was approved by the Lao National Assembly in 2005 but has not been implemented. The decree of implementation is important because it will provide the legal framework for banks and financial institutions to release loans and credit to the business community. MOIC recognizes the problems in enforcing it as it is linked to many other laws.

Labour market and migration

The size of the Lao workforce is estimated to be 1.2 million during the 6th Plan period. These would include 592,000 new labourers; 144,000 active unemployed Laborers from previous years; and 481,000 new unemployed labourers and seasonal job seekers.

The target for job creation during the 6th Plan is set at 652,000 positions with an average of 130,000 jobs per year. Because of data constraints it is difficult to get precise number of jobs created, but it is estimated that ***the level of job creation over the past two years has been low and it may be difficult to meet the 6th Plan target.*** In order to facilitate job creation for more Lao labourers, the Government has initiated the setting up an employment information network on current employment vacancies.

In collaboration with concern sectors and organizations, the fundamental infrastructure of skills training centers have been upgraded from national to local levels. Currently, there are 152 centers throughout the country. ***Attention has been paid to improve the availability and quality of training across the country.*** For example, the vocational training centre in Oudomxay province has opened; curriculum has been updated at the Lao-Korea vocational training center in Vientiane; and a survey on the training needs in the southern region of Laos was undertaken in order to plan for the development of the Training Center in Champasack province. The 6th Plan aims to organize training for 69,300 Lao workers during 2006-10. However, so far only 24,996 people have received training, equal to 36% of the planned target.

Over the past 2 years, the Government has attempted to improve the regulatory framework for the labour sector. The Decree on the Labour Quality Development was submitted to the National Assembly, and is currently being revised. The Labour Law was revised and adopted in the Second – Sixth National Assembly Conference. The Decree on the implementation of the Labour Law was revised and the initial draft is now under review at the departmental level. Research was also conducted on the Instruction on health protection and safety within the construction sectors.

Lao labourers illegally go to work in neighbouring countries and estimating their numbers is a challenge. Based on the coordination on inspecting nationalities with related countries, there are about 99,000 Lao labourers working in neighbouring countries. Of these, about 48,000 of registered labourers were verified as Lao citizens and 28,316 were issued work permits and 20,000 were issued temporary passports.

Four key challenges that need to be addressed relate to: (i) ***provide jobs and incomes***; (ii) ***meet labour skills shortages***; (iii) ***deal more effectively with labour migration*** (inwards and outwards); and (iv) ***better define and implement the labour laws and labour protection.***

Natural resources and the environment

Lao PDR recognizes the potential of its natural resource base for economic development, poverty reduction and food security. This recognition is reflected in the 6th Plan and in the large number of laws, regulations and decrees for sustainable usage (e.g. Hydropower Policy, EIA and SIA regulations, the Fisheries Bill).

The key environmental challenge is to devise suitable ways to benefit economically from its abundant natural resources while at the same time ensuring their sustainability. The economy will continue to depend upon extractive industries, plantations etc. but at the same time, it is important to ensure long-term sustainability of the vast environmental resources. ***There is an urgent need to increase awareness of the need for environmental protection and environmental and health correlations among the general public.*** This requires effective implementation of the National Strategy on Environment Education and Awareness developed in 2004 for the years up to 2020 and Action Plan for 2006-10.

The capacity of various institutions to implement and enforce environmental regulations as well as environmental action plans needs to be strengthened. In addition, there is limited availability of funds to address environmental concerns. The overall budget allocation of less than 1% of total public expenditure for environment is much less than the amount spent on environmental protection by neighboring countries. Donor assistance has bridged some of the financing gap and contributed to a creditable environmental performance of the country.

Science and technology

The Government's focus is on the establishment and development of national science and technology; increasing knowledge; customizing modern technology from foreign countries to local conditions of production, service and infrastructure areas in order to reduce the time for technology transfer and adoption to accelerate its use. It plans to improve research on science and technology; examine and use best practices in science and technology for production and businesses; upgrade the technologies in the main production and services sectors, focusing on increasing the effectiveness and competitiveness of economic sectors; and increase the contribution of science and technology to the overall growth of the country. These will require improvement in the human resource capacities of domestic science and technology including the ability to learn and apply the regional and global innovations.

Lack of budgetary resources is a key challenge in implementing plans of science and technology. There is no budget for research and there are few scientists, knowledge and learned lessons is limited, there is a lack of basic technical materials for research and promotion of science and technology. Private businesses do not invest on the utilization of science and technology in their production and services.

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Infrastructure

The road network continues to improve steadily and is much better and extensive than it was in the previous Plan period. During 2005/06-2007/08, the road network on average grew annually by 2.5% for paved roads, 2.4% for gravel roads, and 3.4% for the entire network.

More than half (52%) of the national roads are paved, but the proportion of paved roads drops sharply for provincial (6.5%) and district (5.1%) roads.

A total of 134 of the 139 district centers are connected to the provincial capitals with all weather asphalt-paved or paved roads. Of these, asphalt-paved roads exist in 47 districts, all-weather paved road in 87 districts and dry season road in 5 districts (3 in Xayabouly and 2 in Attapeu). ***It is unlikely that all districts will be linked by all-year around road access by the end of 2010.***

The most disadvantaged regions in terms of access to roads and social services remain the Central Southern and Northern Highlands and the Northern Lowlands. Much more attention and public support is needed to integrate and link these areas with the overall rural economy. For instance, 5 of 139 district centres (3 in Sayabouri and 2 in Attapeu) need to be connected to the provincial capitals with all-weather paved roads to meet the target to construct provincial roads to link districts. There is a need to increase domestic funds through Road Maintenance Fund for road maintenance.

Air transport

The services at Wattay International Airport have been improved and the airport can now handle about 1.2 million passengers per year. The 6th Plan target is to meet the requirements of 1-1.5 million passengers per year.

Water and Sanitation Supplies

The Plan target is to provide water supply to 59% of total urban households by 2010. ***There are currently different statistics on the coverage for water access because of the different methods used for the surveys. Due to this it is difficult to estimate achievement so far.*** Both the MOH and Water and Sanitation Authority (WASA) are aware of this problem.

Rail Transport

The 3.5 km rail connection with the Thai network and a passenger terminal east of Vientiane in Thanalaeng will be completed in 2008 linking Lao PDR to Thailand.

The transport sector is heavily dominated by the Roads Sector which accounts for almost all domestic movement of people and freight: it is thus to be expected that most expenditure in the sector will be on the maintenance and development of the road network. Investments in other sub-sectors, i.e. waterways, railways and civil aviation are limited reflecting their limited roles.

Total investment on road works, carried out by both private contractors and state-owned construction enterprises, is projected at 73,900 billion kip in the 6th Plan. But ***private sector participation in road works has been increasing in recent years.*** Of the total projected investment, about one-third is to come from the Government's budget. ODA is estimated at US \$357 million per year, and FDI at US \$600 million per year. The resources for MPWT in the 6th Plan are 19,200 billion Kip, or 26% of the total resources. ***The Government faces the enormous challenge of having to provide all-weather basic road access to a large number of villages and to upgrade existing roads to accommodate increasing traffic.*** The available financial resources are insufficient to meet these competing demands. The consistently ***rising***

expenditures for both the transport and the urban sectors for 2005/06-2009/10 make the sector heavily dependent upon donor funds. This emphasizes the need for realism in the budget planning process, as well as for increased prioritization and efficiency of public expenditures, especially in the road sector.

Since 1990, multilateral and bilateral donors together have contributed almost 80% of all public expenditure on roads. However, in recent years, revenues from domestic sources, especially direct user charges, have been increasing steadily. Since its creation in 2001, the Road Maintenance Fund (RMF) has contributed significantly to the quality improvement of the road network. The fund meets 45% of the country's road maintenance needs. ***The RMF funds 60% of the maintenance of national roads, but only 10% of provincial roads, district, and rural roads.*** The Government's target is to raise the fuel levy gradually to 300 Kip/liter by 2008-09. Without donor funds, this increased levy would enable the RMF to cover only the current annual average level of maintenance spending and, by 2008-09, maintenance needs would be more than the RMF could support alone. Increasing domestic sources of revenues is a key challenge for the transport sector.

SECTORAL AND REGIONAL DEVELOPMENT

Agriculture and Forestry

Public investment for the Ministry of Agriculture and Forestry has continued to pay attention and motivate the sector to grow continuously at the average of 4-5 billion kip per annum. MAF developed ***four main goals*** or priority programs for the sector: (i) ***food security***; (ii) ***community crops for domestic and export markets***; (iii) ***stabilisation and eradication of slash-and-burn in the 47 poorest districts***; and (iv) ***sustainable forestry management***. MAF has formulated a medium-term expenditure plan.

Average annual expenditures (public and private) during the 6th Plan are projected to equal 2,360 billion kip (or, US \$24.3 million), for a total of approximately 11,800 billion kip (or US \$120 million) over the Plan period. Spending projections are somewhat lower than previous annual sector spending. The projections indicate that ensuring ***food security and diversification in agriculture and forestry will get approximately 95% of the central capital budget.*** But no provincial breakdown of this national expenditure plan is available.

In 2005/06 the actual state budget expenditure for agriculture and forestry sector was about 477 billion kip. In 2006/07, this is estimated to be about 380 billion kip – a reduction of 20% in one year. This decline is a cause for concern, especially since agriculture is one of the priority sectors for promoting economic growth, employment creation and poverty reduction.

Forestry

Of the public investment, 10-12 billion kip is allocated to the forestry sub-sector. The majority of PIP management and execution (about 60%) is undertaken at the provincial and district levels, with 30% of public investment managed by MAF. All investments support basic infrastructure of agriculture and forestry works (irrigation, research and experiment, station centre), to implement the expected plan based on four objectives of the sector.

Forest and non-timber forest products supplying the domestic market are worth around US \$31.4 million, and about US \$74.4 million worth of products are exported. At present, the industrial and economic tree planting process has increased considerably among all sections of society. Eucalyptus plantations are undertaken in the central region provinces such as Vientiane, Borlikhamxay, Khammuan and Savannakhet. Teak planting covers every province, eaglewood planting takes place in Phongsaly, Vientiane province, Borlikhamxay, Champasak and Attapeu, whereas rubber tree is grown in Northern provinces such as Luangnamtha, Oudomxay, and Bokeo. Neighbouring countries such as Vietnam, Thailand and China have invested in rubber tree plantations.

Irrigation sector

Given the government's continuing emphasis on promoting national rice self-sufficiency, irrigation remains the most important sub-sector in agriculture. ***A large part of public investment is directed toward the construction and rehabilitation of irrigation infrastructure.*** Nevertheless, key issues in irrigation management still must be resolved, including the absence of effective incentives to maintain infrastructure, weak management capacity, and lack of functioning cost recovery mechanisms.

Irrigation investments are targeted primarily to the Mekong Corridor with a strong bias toward Vientiane Province. A recent irrigation investment plan includes the construction and rehabilitation of a total area of 25,800 ha for wet season rice cultivation and 16,800 ha for dry season cropping. This plan covers 10 provinces and a total required investment of approximately US\$ 95 million over five years. While the northern provinces of Oudomxay, Luang Prabang, Xayabury, Bokeo, and Xiengkhuang have received approximately one-third of the actual investment during this period, the majority of the rehabilitation has taken place in the provinces of the Mekong Corridor, namely, Vientiane Municipality, Vientiane Province, Savannakhet, Champasack, and Saravane. Vientiane Municipality received nearly as many funds as all of the provinces in the northern highlands combined.

For stabilising and stopping slash-and-burn cultivation practices, the agriculture and forestry sector has used about 70-80% of the fund which is supported by the state budget, private organizations, projects, international organizations, NGOs and other organizations. These projects have been implemented in 17 provinces, 80 districts covering 303 of village groups for development, in 2,520 villages and 65,056 households nationwide. Projects have been rotated and implemented in many aspects aiming to stop slash-and-burn cultivation practices and allocate permanent occupations related to rural development and poverty reduction works.

Industry

To increase its share of GDP from 26.7% in 2005/06 to 36.4% by 2010, the Government plans to allocate 42% of the total 6th Plan resources to the industry sector. A total of 31,000 billion kip is expected to be invested in the industry sector during the 6th Plan period. Most of these resources are expected to come from private sources or donor partners. It received only 1.2% of the PIP allocation in 2005/06 and 4.2% in 2006/07.

Since October 2005, the total value of manufactured goods has increased by almost 13% per year in line with the 6th Plan target. In the first 6 months of 2007/08 the value of manufactured goods was estimated at about 190 billion kip which is more than 50% of the annual plan. It is expected that by the end of 2007/08 the achievement would double to around 380 billion kip.

Industrial production is continuously growing especially the products for domestic use such as cement, tiles, C packs, iron bars; beer production, soft drink and drinking water. Lao tobacco supply also increased and the achievement against the 6th Plan target is satisfactory. The Katingthong cement factory has a production capacity 3,000 tons of cement per day, or 500-600 thousand tons per year.

A total of 105,234 people were working in the industrial sector in 2006 and the number increased to 105,329 in 2007. The garment factories employ a lot of female labour (about 80%).

While the sector has performed well, serious challenges remain to develop human resources to support the manufacturing sector in order to establish the basic foundations for modernization and industrialization.

There is still insufficient technical equipment for use often because of lack of funds. The future direction is to develop primary factors to modernize the industry.

The garment sector makes up the bulk of exports, but with low value addition of less than 25% of the cost of the product as the majority of raw material is imported. The wood industry is the strength of the nation but is not used effectively and the benefit is not high either. ***Most of the domestic products are imported from abroad such as sugar, iron bars, iron plates and others.*** On the other hand ***there is little investment on transforming the industrial sector, compared to the electrical and mineral sectors.***

The biggest constraint is the quality of the labour force as many are from rural areas and lack working skills. As a result, the cost of the labour is low, and they lack a work ethic and the employees do not have confidence to employ Lao labour. ***For rapid growth of the industrial sector there has to be strong emphasis on developing technical working skills.***

Energy

Significant progress has been achieved in the energy sector in the 6th Plan period. The Plan target is to increase electrical power production up to 2,700 MW. At present the capacity of power production of the existing dams is 671.3 MW. The growth target of electricity production is expected to be 12% per year. The estimate of electrical production capacity during the Plan period is expected to grow slightly because many power construction projects shall be completed and operational by 2009-10.

Four hydropower projects, namely Nam Theun 2 (1090 MW), Xeset 2 (76 MW), Nam Ngum 2 (615 MW), Sekaman 3 (250 MW) are under construction, and expected to start generation by the end of the 6th Plan. Several other hydropower projects are at various stages of planning. The Government has also expanded bilateral power trade agreements with Thailand and Vietnam. Two agreements provide for export of 10,000 MW of electricity to the

neighbouring countries. ***The goal of achieving a single national grid by 2015 is being further advanced by the construction of electricity transmission lines country-wide.*** Operational efficiency is also making good progress. System losses were down to 15.8% by 2007 from a high of 20% in 2005.

Lao PDR's strategic location makes it eminently suitable to become the hub for power trading among the countries in the region. Its hydropower resources provide a unique opportunity to complement the heavy fossil-fuel based generation in the neighbouring countries like Thailand and Cambodia, but also make it increasingly rely upon import to meet its seasonal shortages along with the growth of its system.

The high demand for power in the neighbouring countries, especially Thailand and Vietnam, and the high hydropower generation potential in Lao PDR are encouraging a rapid growth in investment interest in the country. ***A number of constraints need to be addressed to ensure sustainable development of the energy sector.***

Setting suitable export tariff - Domestic electricity demand has increased steadily in recent years and now exceeds available supply. Lao PDR became a net importer of electricity for the first time, and this trend is likely to continue in the medium-term as mining, manufacturing and tourism expand. But currently, ***the import price of electricity is higher than the export price.*** A careful reassessment of the country's power sector requirements is required so as to meet the domestic demand before exporting power.

Financing and quality of investments are major challenges for developing the energy sector - Hydropower sites are likely to become increasingly expensive to develop and their exploitation would depend upon the tariff that major importing countries like Thailand and Vietnam would be willing to pay. In addition, the rising cost of materials is becoming an increasing challenge for the sector. There is an increasing need for investment in the transmission system for interconnection of the four fragmented regional grids and for evacuating power from its rich potential hydropower source. All this results in increasing financial requirements and new sources of funds are needed to meet the 6th Plan targets which may require increased involvement of the private sector.

While attracting investments, it is also important to ***strengthen and enforce a suitable regulatory framework*** and implement the National Policy on the Environmental and Social Sustainability of the Hydropower Sector (2005) to improve the quality of the sector, and build on the successful experiences of Nam Theun 2 and Theun Hinboun power projects.

The capacity of the Government to handle growing investments in the sector remains limited. Financing procedures take a long time to be processed at MOF, which contributes to delays. There is also a strong need to build up capacity of the line ministry and the utility in supply efficiency improvement and demand side management.

Mining

The role of the mining sector in Lao PDR has been transformed fundamentally since the commencement of the first larger scale operation in Sepon in 2003. ***The combined estimated production value of the sector had increased to about US \$800 million by 2007*** from less than US \$10 million in 2002, and ***direct government revenue through taxes, royalties and***

fees exceed US \$120 million. The Government's long-term objective is to develop the minerals sector as a key part of the industrialization and modernization process to help exit the country from the LDC status by 2020.

The mining industry is expected to grow at 15% per year in the 6th Plan period. The mineral sector grew by 1.91% in the first 6 months of 2007/08. *Except for gold all other minerals have already met their 2010 targets.* A total of 109 companies have invested in minerals at present. Of the 171 activities, there are 50 excavations, 72 surveys and 49 activities are excavating for minerals.

A comprehensive review of the Mining Law and status of individual concessions was undertaken in 2007 to cancel inactive concessions. A revised Mining Law is likely to be presented for approval at the National Assembly in December 2008. In the meantime, the Government has imposed a moratorium on new concessions. The current number of valid concessions is around 116 down from more than 120 two years ago.

The success of international operators has underlined the importance of the mining industry and increased expectations of its capacity to contribute to poverty reduction. However, government agencies and the private sector face a formidable task of adapting to a business environment which has expanded manifold over the past five years while staffing levels in government agencies have remained largely unchanged. *Five main challenges for additional and detailed work have been identified.*

Sector governance

A multitude of agencies with overlapping responsibilities are involved in regulation and oversight. As a result, investment negotiations and approval procedures are prolonged and often fail to meet the government's 60-day deadline. The revised Mining Law will lay the foundation for enhanced governance of the sector but more detailed implementing regulation is needed to simplify decision processes and delegate responsibility at various stages of mining operations.

Investment Climate

Presently, there are no standard investment contracts for investment review and approval, although an Indonesian-inspired Mineral Exploration and Production Agreement (MEPA) is used for many large-scale mine negotiations. But the MEPA precedes the Mining Law from 1997 and new standardized contract documents need to be prepared in line with the Mining Law revisions. A full-fledged cadastre management system needs to be developed to track approved investments, ensure adequate planning of new investments, and avoid overlays in concession areas among competing investors. Structured and comprehensive data access is critical to attracting international investors. The sector needs to build the essential foundation for data retention and processing through adequately linked databases and GIS software.

EITI application and mine taxation

As revenue streams from mine operations increase, the public demand for transparency in tax collection and expenditure management will also be growing. The Extractive Industries Transparency Initiative (EITI) is gaining momentum worldwide as an instrument for enhanced transparency in corporate payments and observation of tax obligations. Adoption of

the EITI would at the same time provide reassurance to investors about stability in the investment climate and offer a platform for consultation among national stakeholders and communities.

Capacity building and development of the educational sector

Shortage of skilled labor is a primary constraint to sector growth and even incremental growth within companies already established. The shortage exists at all levels from labor with basic skills to technical competencies through university-level candidates.

Environmental management and community development

There is increased demand for monitoring and supervision of companies' environmental and social performance. Other environmental considerations include potential impacts on habitats, co-existence of mine industries and natural protection programs, mine closure, etc. In the absence of clearly defined land rights there is a strong need for comprehensive consultation and compensation policies and procedures to ensure that new mine operations are undertaken in congruence with locally relevant livelihood strategies, and not at the expense of development opportunities for the project-affected families.

Education

Capital expenditure is expected to progressively decline in 2007/08 and 2008/09 after reaching a peak of more than 60% in the first two years of the 6th Plan period. Consequently, the share of the budget going for recurrent expenditure has increased appreciably in this period. The education sector's share of the 2007/08 recurrent budget is 553 billion kip (of a total budget of 5,442 billion kip) which amounts to 10.2% against a target of 14.0% by 2010. From only 35% in 2005/06, it is estimated to increase to more than 60% by 2008/09. This is a welcome development since if recurrent spending is too low relative to investment, schools will be built but little learning will take place due to a lack of operating funds to pay teachers, buy textbooks, or carry out essential maintenance.

Of the recurrent budget, 90% was spent on salaries in 2005/06 which is estimated to reduce to 84% in 2008/09. Although the share of the recurrent budget allocated to salaries is high, the level of teachers' pay remains a critical issue. Low teacher salaries will have an adverse impact of the quality of teaching as low salaries will either not attract good teachers, or teachers may teach for fewer hours than they are employed to teach because they need time for outside employment to compensate for their very low salaries. It may make it difficult for the government to find teachers to move to poorer and more remote areas. For improving educational outcomes it is necessary to increase the salaries of teachers.

Nearly 90% of the investment in education is financed by donors. This is unsustainable in the long-term. But this may also be an accounting issue where the ODA in education for capacity building or training is measured (correctly) as investment in conceptual terms, but *de facto* the funds are administered and spent as though for recurrent items.

From the data available for 2007-08, there is a mis-match between the national priorities and the resources allocated for the sub-sectors. ***Less than 1% is allocated for early child care and education.*** Administration and management is the single largest recipient of government's

recurrent expenditure, and could be a result of mis-allocation. The allocation data needs to be re-evaluated to correctly understand whether and to what extent do the Plan priorities receive sufficient financial resources.

Provincial and local administrations have the core responsibility to deliver primary and secondary education. But there are no standardized cost formulae (apart from broad guidelines on, for example, teacher ratios) that the provinces could apply on a consistent basis. ***There is nothing in the current transfer system to ensure compliance with overall national policies or to even out spending disparities among provinces.***

There have been a number of achievements in the education sector during the first half of the 6th Plan. These include improvements in key indicators such as net enrolment rates in primary education, which have risen from 83.9% in 2005/06 to 89.2% in 2007/08 towards a target of 90.6% by 2010. Others are:

- Reform of teaching and learning methodologies
- Revision of the pre-primary and primary curricula
- Introduction of the 5-4-3 system of schooling
- Improving the quality of teachers
- Construction of learning institutions
- Quality of education
- Community participation
- Administrative Restructuring
- Training of staff
- Setting unit cost norms

Efforts to reduce the cost burdens on the poorest families are also being undertaken through drafting legislation on exemption of tuition fees as well as providing incentives for poor families, especially girls, in target villages to help them with the direct costs of schooling (uniforms, learning materials etc). Thus, progress in terms of the legal and administrative processes is good and will need to be matched by similar developments in actual flows of funds if the targets are to be achieved.

All the same, the education sector faces a number of challenges.

Lack of an overarching strategic plan to define priorities, guide resource allocation and ensure balanced development of the sector and slow progress in moving towards a Sector Wide Approach (SWAp) for the sector. Recognizing this key constraint, MOE has embarked upon the production of the Education Sector Development Framework (ESDF) which will set out the policies, strategies, implementation plans, monitoring systems and overall financing plans and costs for the next 10 years.

Slow progress against EFA goals that require renewed efforts to tackle some of the key issues such as access to basic education, drop-out and repetition rates.

The majority of the recurrent budget is used for salaries with very little left over to actually support the reform of the system. Donors and community contributions therefore provide funds to support what would normally be considered to be items under a government's recurrent budget.

The overall low level of Government spending in education along with the unequal allocation of scarce resources continues to impact heavily at provincial, district and school levels. Provincial governors still maintain high degrees of autonomy in terms of public spending. In effect this often means that provincial level priorities take precedence over national strategies and thus although policies may be in place to target pressing education issues, in reality resources may be allocated elsewhere.

The education system relies heavily on the only annually nationally available data set produced by the Education Management Information System (EMIS). Numerous changes are needed to strengthen the system including recruiting more staff, investing in new technology and establishing official school catchment areas. These will help improve the quality and speed with which data can be collected, analyzed and disseminated. EMIS needs increased levels of support from MOE and the donors.

Capacity, both of the system as a whole and of individuals, continues to be a constraint hampering the education sector's ability to fully achieve 6th Plan targets. MOE is a large and complex organization which has the government's largest civilian workforce. Lines of communication and authority vary from those which are centralized (such as the budget allocation, management of personnel and curriculum development) to those which are decentralized (such as teaching). Coordinated and systematic capacity development to fulfill 6th Plan aims is needed in terms of management, pedagogy and administration.

Despite the progress of the Education Sector Working Group (ESWG) and momentum generated by the on-going development of the ESDF, ***provincial level coordination of development partner interventions is mixed.*** There are still a large number of on-going projects with often similar mandates and/or coverage areas. More work needs to be done to assist provincial and district authorities to consolidate similar activities and coordinate inputs and support at school/district/provincial levels.

The mid-term review of the 6th Plan indicates that there has been considerable progress towards achieving the 2010 targets in education. However 10 key priorities, consistent with the recent EFA MDA report and draft school sector inputs of the ESDF, emerge:

- provide access to primary education for children, especially in remote rural areas, and increase participation in lower secondary education;
- make the primary sector more efficient through reduction of repetition and drop-outs;
- design programs which allow school failures and drop-outs to re-enter the education system to realize their potential;
- reduce the cost barriers to education for children from the poorest families through the School Feeding Project and/or scholarship programmes;
- encourage parental support for, and active involvement with, their children's education;
- develop a curriculum responsive to local needs;
- improve the quality of primary, secondary and tertiary education so that the outcomes match the needs for a skilled population able to participate in the global economy;
- ensure access to quality education of disadvantaged groups including females, those with physical and mental disabilities, and those who do not speak Lao;
- enhance the collection, management and dissemination of data for education planning and evaluation of the impact of 6th Plan policies; and

- provide sustained technical expertise at different levels to assist in translating the broad strategic directions in the ESDF into annual management and implementation plans to ensure activities actually take place in support of the above goals.

Health

The overarching goals of the health sector for the 6th Plan are to:

- develop a nation-wide health delivery service that is fair and equal according to gender, age, social rank, tradition, religion, ethnicity, and geographic location;
- provide basic health services that respond to the peoples' needs and expectations and that gain the peoples' trust; and
- achieve substantial improvement in peoples' health status, especially of poor people.

Although health financing should be prominent, the issue is hardly mentioned in the Plan document. Health spending as % of GDP will increase from 1.65% to 1.98% over the 6th Plan period. This is in spite of the decline in private financing which is likely to show a 25% decline in this period.

The Government has relied heavily on external financing for public health and preventive programs, especially operational expenditure. The Hygiene and Preventive (H&P) programs are key to delivering essential public goods in the health sector and account for a substantial portion of total health spending.

Capital expenditure accounts for about 55% of government health expenditure during 2005-07 but is likely to constitute 72% in 2008-09. This is up from nearly 40% during 2002-05. Lao PDR has been overspending on capital investment. These increased inflows of capital investment will exacerbate the current shortfall of recurrent expenditures to operate existing facilities due to additional demands for recurrent expenditures.

There will be a significant gap in financing for health sector recurrent spending as the projections for health public expenditure considerably exceed the available resources. This will require dependence on donor funding. MOH estimates that the funding needs for staff and salary increases alone will be close to US \$13 million by 2010, even assuming that the necessary levels of external funding are forthcoming. An additional gap will exist in non-wage recurrent spending.

Even though domestic health expenditure is likely to go up from US \$1.8 per capita per year in 2005-06 to US \$3.7 per capita per year in 2008-09, it still remains among the lowest in the region.

The considerable reliance on out-of-pocket expenditures for funding the health system seriously affects the poor, especially those living in rural areas amongst whom cash flow is limited. Consequently, the people without cash at hand delay or avoid treatments, resort to self medication or consult traditional healers.

Malaria, tuberculosis and HIV National programmes rely mainly on Global Fund funding mechanism. So far Lao PDR has been very successful in attracting funding from the Global

Fund and by end-June 2008, Global Fund funding for the 3 diseases had reached a total of US \$94 million.

A number of social protection schemes are implemented to limit the negative effect of the high out-of-pocket expenditure to finance the health services. All these schemes depend to a large extent on donor funds to operate.

Overall there has been steady progress in the health sector in most of the areas highlighted in the 6th Plan. As part of the MOH's bottom-up approach for strengthening the country's health services seven priority areas for primary health care (PHC) have been identified in line with the "Model Health Village Program". The seven declared priority programmes and strategies of PHC for the 6th Plan period are:

1. Primary health care (PHC) service delivery
2. Health promotion & information, education & communication (IEC)
3. Maternal & child health (MCH), immunization, nutrition & population
4. Water supply & environmental health
5. Communicable disease surveillance & response (CSR) including malaria, dengue, cholera, tuberculosis & helminthes, HIV/AIDS & avian influenza
6. Health systems strengthening with a focus on health financing and human resources and
7. Health sector-wide coordination.

Building adequate human resource capacity is a key challenge for the health sector. MOH is committed to expanding human resource for health (HRH) and several major activities have been conducted to increase human capacity in the health sector.

Tourism

Tourism is a key sector driving the country's economic growth and is ranked as among the top two foreign exchange earners. It was identified as a priority export sector under the National Export Strategy 2006-2008.

Under the 6th Plan, the government expects the number of tourist arrivals to reach an estimated 2.3 million in 2010 up from 1.6 million in 2008 and 1.4 million in 2007, and generate about US \$233 million in direct revenue. Most tourists come from the ASEAN region (Thailand, Vietnam, and China), Japan, North America (USA and Canada), Europe (France, UK, and Germany), and Australia. With increased regional and international integration the tourism sector is expected to grow at about 8-10% annually.

The tourism sector accounts for approximately 8% of overall GDP and is a major employer, directly employing about 17,000 workers and indirectly about 50,000-100,000 people, mostly from local communities.

To achieve the 6th Plan targets, the government launched the Tourism Strategy (2006-20), which defines the policy guidelines and overall goal to develop and promote the sector. The role of the sector has been boosted by a recent Party Congress resolution aimed at strengthening and developing the sector to increase foreign exchange revenues and provide opportunities (employment and regional integration) for local and urban areas.

There has been an impressive growth of tourism infrastructure in the 6th Plan period. The number of tourist companies grew by about 80%, whereas the number of hotels and guesthouses increased by more than 25% between 2005/6-2007/08.

In addition to the growth of the private sector in tourism development, the government has taken a number of steps, with support from development partners, to encourage tourism in the country. Specific achievements during the past 2.5 years include:

- Construction of basic infrastructure
- Increased border access
- Provision of tourism information and services, marketing and promotion
- Improvement of the organizational structure of LNTA and PTA
- Human resource development
- Tourism Strategic Plan for 2006-20 endorsed by the Government in March 2007
- Development of Tourism sites
- Ecotourism Development
- Collection of tourism-related statistics
- Endorsement of the Law on Tourism.

Some key challenges remain:

Insufficient staff is provided to various Departments compared with the current volume of work. The number of tourism officials responsible for advertising and promotion is also limited and the quality of the tourism websites does not compare favourably with international standards.

The organization structures of Tourism Offices of some provinces have not been systematically developed.

The system of collection of research information is weak due to use of improper tools for conducting research. Monthly reporting on tourist statistics by provinces with border check points is often late. ***Implementation of tourism development plans of provinces is delayed and does not meet the needs for development in each province.*** Some projects have been put in the plan of the year but cannot be implemented due to a lack of budget.

The printing or publishing of advertising were not sufficient compared with the needs of tourists. The advertising papers are not written in many languages, and the advertising does not focus on the local market. i.e. Lao visiting Laos, there are not many advertisements written in Lao language, equipment and facilities provided to the Tourism Information Centre at central and local levels are not modern, the budget for advertising is limited.

There are insufficient trainers in the Training Centre of the Lao National Tourism Administration. Most provinces are unable to organize training/workshops by themselves especially on the area of hotel operations.

Key priority area for the sector is to establish and strengthen partnership with the private sector which plays a dominant role in the tourism sector and local communities for a new tourism development pattern to: (i) improve the sustainability of natural, urban and cultural angles for tourism; (ii) create new tourism products that would benefit the poor; (iii) tap the opportunities offered by the recently completed GMS transport corridors to promote tourism;

and (iv) enhance human resource capacities in tourism SMEs/PS and among public sector officials to improve the competitiveness and quality of service.

More attention is needed on the investment and business climate through regulation and principles to support the private sector and foreign investors who want to enter the tourism sector. Cross-sector collaboration/coordination among core sectors such as education, health, communication and infrastructure needs to be enhanced.

Promoting gender equality is an important national goal of the government as reflected in the 6th Plan. Women are commonly employed in the tourism sector and ***there is need to pay more attention in enhancing and creating opportunities for women through promoting women's participation in the tourism-related business activities including in areas such as handicrafts production and sales.***

Regional Development

Between 2005/06 and 2007/08, total PIP administered from the provinces was 2,747 billion kip, which represents approximately 50% of total PIP expenditure. ***On aggregate, implementation of the PIP has occurred in a timely manner***, with actual expenditure at 82% of planned expenditure during 2005/06 - 2007/08. However, ***the delivery rate of ODA against planned was significantly lower than domestic funds. This is primarily due to the fact that ODA projects are often large projects and therefore more susceptible to delays.***

There is significant variance across regions in term of per capita PIP expenditure. In the northern region, PIP per capita expenditure is 252,000 kip per person, compared to 144,000 kip per person in the southern region. ***This discrepancy is primarily caused by the discrepancy in ODA flows to the different regions, which again highlights the need for stronger ODA coordination.***

Priorities for 2008/09 and beyond include:

- **Land management** - The significant increase in investment in commercial agricultural and tree plantations has underscored the urgent need to speed up the government's land reform process (land titling, land zoning, investment regulations regarding compensation and resettlement) to ensure efficient and effective use of land for productive purposes, and equitable access to land.
- **Forestry** - Strict implementation of the Prime Minister's decree on the banning of log exports is necessary. Increase public resources to the forestry sector, particularly at the provincial level for the management of the National and Local Protected Areas.
- **Industry** - Focus on industries other than the large mining and hydroelectricity projects.
- **Education** – While there has been an improvement in the availability and quality of vocational training institutions across the country, more attention needs to be given to the development and successful operation of vocational training centres and technical colleges in the provincial capitals.
- **Infrastructure** - Priority should be given to constructing all-weather roads to Phongsalai, Sayabouli and Salavan provinces.
- **Tourism** - Continue to support the eco-tourism program managed by the PTAs in the 10 provinces, and expand to other provinces as appropriate. Give priority to establishing the

tourism training centre in Vientiane, as well as establishing courses in the northern region (through Souphanouvong University) and the southern regions.

- Aid Coordination and Effectiveness - Urgently upgrade the existing aid information management system and strengthen capacities at the provincial level for better aid coordination and management.

MONITORING AND EVALUATION MECHANISMS

Monitoring of the 6th Plan requires a comprehensive M&E system for the government to track progress and use the information for policy making. However, the M&E function is currently divided amongst four principal actors within the government with varied M&E responsibilities and little coordination.

MPI monitors the overall implementation of the 6th Plan and reports to the National Assembly on a bimonthly basis. It also prepares and presents an annual performance report on plan implementation. The information collected from the line ministries, agencies and provinces is largely descriptive and incomplete, posing a major challenge for Department of Statistics (DOS) operating under MPI to compile adequate monitoring data.

The Department of International Cooperation (DIC) monitors ODA projects, capturing the commitments of donors on disbursements. This reporting is based on commitments and actual disbursements using available data at MPI and from MOF, line ministries, PIUs and DPs. Some discrepancies are noted on what is meant by disbursement by the government and the development partners as stated in the OECD/DAC Survey 2008.

MOF monitors all loans as well as technical assistance tied to the loans. The Bank of Laos monitors debt and debt repayment. In addition, the Department of International Organizations of MoFA is in charge of monitoring projects and programmes by international NGOs.

At the development outcome level, DOS captures trends in development indicators through surveys and censuses. It undertakes the monitoring and evaluation of the outcomes and impacts of the plans by establishing a uniform and consistent national database on economic, social and governance indicators. In consultation with relevant Government agencies, it has prepared a list of about 100 core indicators that could be utilised to monitor the impacts of the Plans, MDGs and the Brussels Programme of Action for Least Developed Countries (2001-2010). Many of these indicators are incorporated in the LaoInfo 4.1 database. However, monitoring the 100 core indicators has proved to be cumbersome. In addition, DOS undertakes a small sample survey annually as well as a full income and expenditure survey every five years. The results are also incorporated into LaoInfo database.

The present system of implementation monitoring faces a number of challenges:

- Line ministries, agencies and local authorities have limited capacities in preparing comprehensive evidence-based reports.
- Most reports prepared are often incomplete and the information is descriptive.
- The coverage of the reports and the quality of the information vary widely.

- Both skills and equipment including communications and computer facilities need improvement.

In general, a number of constraints affect monitoring of the 6th Plan

- lack of reliable data;
- little coordination between line ministries and agencies;
- inadequate human and financial resources for data collection and analysis;
- insufficient appreciation of M&E as a management tool; and
- uncoordinated and cumbersome M&E requirements often presented by donors in connection with their projects.

Building upon the existing system and strengthening the links and capacities at all levels are urgent matters for the government in order to develop an effective Monitoring and Evaluation (M&E) system for the 6th Plan.

Monitoring of ODA-funded projects

The need for effective coordination and management of foreign aid is increasingly recognized by both donors and the government. Arising from the Vientiane Declaration and the associated Country Action Plan, most donors have agreed to align their work programmes with the national priority sectors of 6th Plan. The government has improved its mechanisms for streamlining aid coordination.

MPI is currently in the process of establishing a suitable ODA database management system to track all ODA resources and to record and provide information on progress of all development programmes in the country. The new system will also need to serve all line Ministries' purposes to keep track of all ODA inflows and the results. The challenge here is for development partners to make aid commitments and disbursements more predictable and accurate and for the Government to improve ODA management which implies, among other things, strengthening inter-ministerial cooperation and building required capacities.

A standard Financial Management Manual is being developed by the Ministry of Finance to provide guidance on harmonized procedures for different financial management steps of ODA projects and programs (budgeting, accounting, internal control, disbursement, reporting and auditing). This manual is intended for all government staff working in ODA projects and programs.

Greater predictability of ODA will help improve the national planning, programming and budgeting processes. ***The round table process with the associated sector working groups is the major channel of donor coordination in Laos.*** The round table meeting (RTM) is the highest level of donor coordination between the Government of Lao PDR and its development partners.

GOL seeks greater donor coordination and harmonization of foreign assistance through joint Government-donor working groups in support of policy reform as well as investments in health, education, infrastructure and agriculture. As part of the RTM process, the government established eight Sector Working Groups (SWGs) in June 2005 to facilitate aid coordination at sector and thematic area levels, and to enter into direct dialogue with the

donors. Apart from the UN agencies, international financial institutions (IFIs), most donors, and international NGOs have nominated representatives to the SWGs. Chaired and led by the Government, and with broad participation from various government and other agencies, these working groups reflect the jointly identified development priorities:

- Education
- Health
- Infrastructure
- Macro-economic issues and private sector development
- Agriculture, rural development and natural resources management
- Governance
- Drug prevention
- Mine action

Overall, the structure and substance of the SWGs is varied. *There has been concern about the SWGs losing momentum, lacking a clear mandate and a work plan.* Recognising this constraint DIC has attempted to restructure and reorganise the SWGs. Over the past few months TORs have been prepared for all SWGs although only a few have Annual Work Plans with targeted results and measurable indicators.

CONCLUSION

Priorities

The 6th Plan (2006-10) is fairly comprehensive and well-prepared that aims to achieve the MDGs, and plans to set the country on track for exiting the LDC status by 2020. It covers all the areas relevant to the development of the country and envisages poverty reduction through a combination of broad-based economic growth and focused and policy interventions. The 6th Plan document establishes that economic growth must be linked to social progress and equity, cultural development and environmental conservation.

The priority sectors have been correctly chosen. But there is little elaboration on sub-sectors in the Plan document. This has serious implications for developing priorities and allocating resources.

Continued success in poverty reduction will depend largely on the extent to which it can extend to all sections of society and to the remote regions in the country. Public spending has made an important contribution to growth and poverty reduction, particularly in priority poorest districts. But *Lao PDR's prospects of achieving its development goals over the long-term depend ultimately on the growth of the non-resource sectors and the extent to which they can generate employment.*

The 6th Plan recognizes the importance of sustainable environmental and natural resources management for the development of Lao PDR. Along with the National Strategy on Environment (2003-20), it embraces the MDGs, linking economic well-being and social development to environmental sustainability. In addition, the 6th Plan recommends integrating and mainstreaming of gender concerns in key sectors such as agriculture, health,

education and the strengthening of the Lao National Commission for the Advancement of Women (NCAW). These are welcome developments.

All the same, *there is only a single mention to malnutrition as part of the chapter on poverty reduction* where a target is set for reducing the number of malnourished children over the Plan period. This is a likely consequence of a mis-perception that poverty reduction alone is sufficient to reduce malnutrition. This is being rectified through the recent National Nutrition Policy that will be presented to the National Assembly in November 2008.

In many respects, *the 6th Plan is MDG-oriented but not MDG-centric*. It does not place meeting the MDGs as the focus of activity and there is no clear strategy as to how the MDGs will be met by 2015. The objectives set out in the strategy support the achievement of the MDGs; and the indicators and targets of the plan coincide with most of those for the MDGs. But the 6th Plan is not MDG-based even though the MDG targets have been localised to reflect Laotian reality. It is hoped that this will be rectified at the time of formulation of the 7th Plan which will be the last one before the 2015 deadline for meeting the MDGs.

Resources

There is considerable under-provisioning of social sectors - the health sector gets less than 2% and education only just above 3% of the GDP. Public spending in health and education, after reaching a high of 3.8% of GDP in 2005/06 and 2006/07, is estimated to decline to 3.3% by 2008/09. This is due to declining donor support which maybe in anticipation of future resource flows from NT2 and other projects, or the introduction of VAT in January 2009 which is likely to increase domestic revenues. But the decline may affect enrollment levels in primary and higher education and limit the ability to improve the quality of its workforce and respond to the needs of a globalised and integrated economy.

Also *there is some inefficiency in resource allocation*. For instance, more than half the resources were allocated for capital expenditure in 2005/06 and 2006/07. These increased inflows of capital investment will exacerbate the current shortfall of recurrent expenditures to operate existing facilities.

Majority of the recurrent budget is spent on salaries, leaving limited funds for actual implementation. Actual implementation is undertaken using ODA funds which can be unsustainable in the long-term.

A key limitation of the 6th Plan is that it is loosely linked to the budgetary process.

It is not clear whether all the activities listed in the various sections can be funded with the available resources.

While the priority sectors have been correctly chosen and the Plan is strongly poverty-focused, there is an urgent need to improve domestic revenue and the budget system.

Expenditure on priority sectors so far is insufficient to meet either the 6th Plan targets or the MDGs.

There is an urgent need to strengthen the integration of planning and budgetary processes and reorient public expenditures in the remaining period of the 6th Plan.

Implementation Process and Institutional Mechanisms

The 6th Plan sets a number of ambitious goals and targets both overall and for different sectors, but without a clear strategy of how these will be met. Ideally, the Plan should be accompanied with strategies for different sectors that describe how the various targets for the different sectors shall be met, and how the resources will be allocated. Some departments have worked to develop sectoral strategies, but often these were developed a few years after the Plan was already being implemented and then, their time horizons went beyond the 6th Plan period of 2006-10. While there was an overlap between the two, it wasn't always clear as to what was being implemented at a particular time – the 6th Plan or the sector strategy.

Programmes are generally managed and directed by the Ministries but actually implemented largely by provincial and district offices. This often leads to a mis-match between national priorities and resource allocation by provinces. Specifying a minimum per capita budget allocation the provinces for different sectors would ensure overall resource allocation to reflect national priorities.

Low human resource capacity is a key factor impeding the successful implementation of the 6th Plan and achieving various targets

The 6th Plan includes a poverty reduction strategy and the MDGs and is implemented through regular development programmes of the sectors, provinces and districts through the Annual Plans and Budgets. The targeted programmes are implemented largely through the existing systems. Together, this requires considerable capacity strengthening at all levels given the modest capacities of the public administration overall and at the grassroots. This is necessary to ensure the sustainability of implementation of the strategy.

Strengthening human capacity remains a high priority

The 6th Plan highlighted the commitment by the Government to continue the reform of the civil service, with a view, among other things, to addressing the issue of salaries of public servants. The Government is also committed to establishing an efficient social security system for all Lao people and, assures to implement the policy on salaries and support the provision of incentive payments to staff working in remote areas.

Lack of an effective monitoring system

In spite of considerable progress in meeting the targets objectives, monitoring of progress of the 6th Plan has been weak. It is difficult to get an overall objective picture of implementation. This is because it is difficult to get reliable and timely data. Lack of reliable data has been a major constraint in economic planning, resources budgeting and management, policymaking and progress monitoring in Lao PDR.

The 6th Plan presents a sound MDG-based summary targets table, but lacks a fully-fledged monitoring and evaluation framework linking input, output, outcome and impact indicators for each sector so as to allow for proper monitoring. Developing such a

framework is critical to exploiting the Plan's potential as a tool for monitoring results, improving accountability and feeding back lessons learned and useful information into policy making. The link from sector policies to resources, outputs and indicators to the final impact targets as well as baseline data is often missing.

In the next years, it is necessary to improve monitoring mechanisms for district expenditure to assess the effectiveness of the poverty strategy. Provincial line agencies should start screening their expenditure by district for better targeting in the poverty strategy programs.

Progress

The macro-economic fundamentals of the Lao economy are sound. Lao PDR's economic performance continues to be strong. Growth is robust and has been in line with the targets set at the start of the 6th Plan. Inflation is within acceptable limits, reserves have risen rapidly because of strong tourism receipts and resource exports which, combined with high FDI and ODA inflows, resulted in a substantial surplus. Consequently, poverty has declined sharply over the last 10 years and headcount poverty level in 2007 may be below the 30% level. Thus, *the overall economic outlook is promising and if managed well, can help achieve many of the Plan targets.* However, certain concerns persist which require attention. These have been discussed at various places in the main review report.

Reviewing achievement of implementation of the 6th Plan has an important limitation. Progress only in terms of resource allocation or physical achievements can be assessed. It is difficult to assess progress on outcome indicators such as poverty, malnutrition, literacy, life expectancy, infant and maternal mortality because the collection of data for these indicators takes place with the help of sample surveys once every three to five years. For many indicators, the most recent published data preceded the start of the 6th Plan and hence can be used only as a baseline, and not to review progress. Also, outcome indicators change slowly over time. Even if data was to be collected each year for measuring changes in mortality rates, there would be little or no change in the mortality rates on a year-to-year basis.

Consequently, a more prudent strategy adopted for the mid-term review is to focus on priorities, budgetary resources and implementation processes to analyse how well these contribute to achieving the 6th Plan goals. Being able to identify gaps and strengthen the systems would contribute greatly towards better implementation in the remaining period of the 6th Plan and in the 7th Plan (2011-15).

DIRECTIONS OF THE 6TH PLAN AND FOCUS AREAS FOR THE NEXT 2.5 YEARS

The remaining period of the 6th Plan could pay particular attention to the following:

Aim for a 7.5-8% GDP growth with an emphasis on the growth of industry and the services sectors. Efforts need to be made to increase agricultural output and employment in agro-processing and off-farm activities. The business environment needs to be strengthened, including those areas that particularly affect development of SMEs.

Maintain inflation at less than 10%. Priority strategies will include encouraging sufficient domestic food production, maintaining manageable trade deficit and import of only necessary goods, and maintaining a control over monetary policies.

Maintain budget deficit at an appropriate level by focusing on strengthening revenue generation and adopting prudent government expenditures in line with priorities. Focus on implementing the State Budget Law, in particular the reforms to taxation, custom and treasury and the reforms to strictly monitor the financial management and accounting of various agencies and enterprises at all levels, and the debt liability committee to manage the inspection of the debt in public investment projects.

Focus on developing stronger inter-sectoral links between agricultural and manufacturing sectors, repair the damaged irrigation system in order to ensure the supply of water for agricultural production; encourage banks to support agricultural production and manufacturing. Implement the Order No. 31/PM on management of forest and wood business.

Improve the efficiency and effectiveness of public investment projects, in particular the implementation of a monitoring and evaluation system; revise the law on Public Investment in order to upgrade the effectiveness and efficiency in management. Review the effectiveness of the 11 national priority programs to aim for a better alignment of these programs with the public investment projects.

Implement the Country Action Plan of the “Vientiane Declaration on Aid Effectiveness”. Donors should aim to reduce aid volatility. There is an urgent need to strengthen the donor database so as to get a better sense of aid flows in the country.

Strengthen the regulatory environment to attract more foreign investment, including rolling out the one-stop-shop service effectively.

Continue to improve the legal framework related to the granting of land concessions, surveying rights, and the export of mineral products for ensuring the highest benefits.

Implement policies that can attract teachers to work in remote areas; encourage and promote private sector to participate more in human resource development; improve the quality of normal education and college level to gradually reach international standards, attempt to implement 4 priority projects of education sector to achieve the targets.

Improve and upgrade the quality of health care treatment and services at large hospitals at central level and provinces to international standards; improve the quality of services in order to build confidence for people who use the services; construct new health care centres in local areas which do not currently have a centre and improve the existing health care centres to meet the standard in order to be able to provide services on basic health care treatment; operate the actions for combating the infection of dangerous diseases in timely manner.

Continue to build foundation for rural development and eradicate poverty by taking the building of villages and development village groups as central task according to 4 contents and 4 target goals. Provide funds in village groups or focal development areas where there are necessary; actively implement the policies and projects especially village development funding, Nayobay Bank, Poverty Eradication Fund and other development funds of sectors and local level effectively.

In addition, it would be useful to focus on strengthening systems that not only improve the achievement of 6th Plan objectives, but also haven impact on the success of the 7th Plan. These include:

Set up of a comprehensive M&E system which while would also be an excellent resource for developing baseline indicators for the 7th Plan

Developing a functioning M&E system is essential to meet the monitoring and reporting requirements of the 6th Plan and other developmental plans, and provide information to assist in planning and decision making at various levels. The M&E system may be labeled as Central Monitoring and Reporting System (CMRS) to reflect its scope. It can be integrated with the existing Management Information Systems (MIS) and statistical systems of line ministries to provide requisite data/information about both the MDG and 6th Plan indicators.

Developing fully costed Sector Strategies for sectors which have not done so far

The sector strategies should be accompanied by detailed costing exercise to get a sense of the resources required to achieve the Plan objectives as well as the MDGs. The period of the 7th Plan which goes up to 2015, shall be the last opportunity to work towards achieving the MDGs. In that sense it is important to ensure that the sector strategies are aligned with the MDGs. Alongside, a set of indicators and time-bound annual targets should also be developed to assist in systematic monitoring of progress. This would be helpful not only for the remaining period of the 6th Plan, but more so for serving as baseline indicators for the 7th Plan. The SWGs may take the lead in developing the sector strategies. In addition, a system of budget norms need to be developed that will ensure that budget allocations are based on sector strategies and that the budget becomes an instrument of public policy.